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### U.S. Supreme Court Draws Bright Line on Application of Securities Exchange Act of 1934 to “Foreign Cubed” Transactions

In a decision likely to have wide-ranging implications in the area of securities fraud litigation, the United States Supreme Court has significantly restricted foreign (and potentially domestic) plaintiffs’ access to U.S. courts to assert securities law violations against non-U.S. companies. In *Morrison v. National Australia Bank Ltd.*, 210 U.S. LEXIS 5257, (Jun. 24, 2010) (“*NAB*”), the Supreme Court established a bright line rule that allows a private cause of action under the Securities Exchange Act only if “the purchase or sale [of a security] is made in the United States, or involves a security listed on a domestic exchange.” *Id.* at \*39.

In *NAB*, non-U.S. purchasers of ordinary shares of National Australia Bank, a corporation headquartered in Australia and incorporated under Australian law, brought suit against the bank and its officers alleging violation of Section 10(b)(5) of the Securities Exchange Act of 1934. They alleged the defendants made materially false and misleading statements in SEC filings, annual reports and press releases regarding the profitability of *NAB*’s U.S. home loan servicing subsidiary, HomeSide.

In this example of a “foreign cubed” action (foreign plaintiff against foreign defendant regarding foreign securities), the Court of Appeals for the Second Circuit noted “when faced with securities law claims with an international component, we turn to ‘the underlying purpose of the anti-fraud provisions as a guide’ to ‘discern whether Congress would have wished the precious resources of the United States courts and law enforcement agencies to be devoted to’ such transactions.” *Morrison v. National Australia Bank*, 547 F.3d 167, 170 (2d Cir. 2008) (internal citations omitted).

To determine this Congressional intent, the Second Circuit looked to whether the harm was perpetrated in the U.S. or abroad and whether it affected U.S. markets and investors. *Id.* These two tests, referred to as the “conduct” and the “effects” tests, were frequently applied together “because an admixture or combination of the two often gives a better picture of whether there is sufficient United States involvement to justify the exercise of jurisdiction by an American court.” *Id.* at 171.

A majority of the Supreme Court justices specifically rejected the Second Circuit’s “cause” and “effects” tests on the grounds that it was error to attempt to determine Congressional intent instead of determining, as it must, whether the Act clearly indicated that it was intended to have extraterritorial application. 210 U.S. LEXIS 5257 at \*24-25. The Court confirmed that “[w]hen a statute gives no clear indication of an extraterritorial application, it has none.” *Id.* at \*15.

Under this presumption against extraterritorial application, the Supreme Court held the Securities Exchange Act applied only to transactions involving securities listed on U.S. exchanges or to purchases or sales in the U.S. of non-listed securities. *Id.* at \*32. In so holding, the Court noted “the focus of the Exchange Act is not upon the place where the deception originated, but upon purchases and sales of securities in the United States. Section 10(b) does not punish deceptive conduct, but only deceptive conduct ‘in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered.’” *Id.* at \*34. The location of the alleged fraudulent acts and the effect on U.S. investors or markets were irrelevant to this statutory construction and were accordingly rejected as relevant criteria. *Id.* at \*24. Plaintiffs’ suit against *NAB* and its officers was dismissed for failure to state a claim.

The Supreme Court emphasized that its new bright line rule would provide predictability and prevent conflict with the securities laws of other countries. *Id.* at \*24-\*25. Under this new test, both U.S. and non-U.S. investors may be precluded from maintaining section 10(b)(5) fraud suits against non-U.S. companies where the company’s shares are not listed on a U.S. exchange or were not purchased in the U.S. This decision is likely to have a far reaching impact given the volume of securities litigation in U.S. courts.

If you have any questions concerning this decision, please do not hesitate to contact us.

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